

Internal Revenue Service

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September 20, 2012

Legend

X =

State =

Date 1 =

Date 2 =

Dear _____ :

This letter responds to a letter dated April 24, 2012 submitted by X's authorized representatives on behalf of X, requesting a ruling under § 1361(b)(1)(D) of the Internal Revenue Code.

The information submitted states that X was incorporated under the laws of State and subsequently made an election to be treated as an S corporation effective Date 1. X and its shareholders intend to enter into an agreement ("Agreement") effective Date 2 which contains provisions relating to minimum distributions to shareholders by X. X and its shareholders intend that X will make distributions under these provisions based on the shareholders' varying interests in X's income in the current or immediately preceding taxable year ("Varying Interests Distributions") or earlier if such earlier year's taxable income is adjusted after X's original return for the such earlier year is filed ("Discretionary Payments"). X and its shareholders intend that the Varying Interest Distributions will include year-end and quarterly distributions that enable the shareholders to make timely estimated and final tax payments.

In addition to above distributions, X may declare dividends and make pro rata distributions to the shareholders based on the number of shares that the shareholders

own as of a record date (Record Date Distributions). The Agreement will provide that X will make these Record Date Distributions in accordance with the corporate laws of State, which provides that all shares of the same class are equal.

Section 1361(a)(1) provides that for purposes of the Code, the term “S corporation” means, with respect to the taxable year, a small business corporation for which an election under § 1362(a) is in effect for the year.

Section 1361(b)(1)(D) provides that the term “small business corporation” means a domestic corporation that, among other things, does not have more than one class of stock. Accordingly, S corporations may not have more than one class of stock.

Section 1.1361-1(l)(1) of the Income Tax Regulations provides that a corporation that has more than one class of stock does not qualify as a small business corporation. Except as provided in § 1.1361-1(l)(4) (relating to instruments, obligations, or arrangements treated as a second class of stock), a corporation is treated as having only one class of stock if all outstanding shares of stock of the corporation confer identical rights to distribution and liquidation proceeds.

Section 1.1361-1(l)(2)(i) provides, in part, that the determination whether all outstanding shares of stock confer identical rights to distribution and liquidation proceeds is made based on the corporate charter, articles of incorporation, bylaws, applicable state law, and binding agreements relating to distribution and liquidation proceeds (collectively, the governing provisions). Although a corporation is not treated as having more than one class of stock so long as the governing provisions provide for identical distribution and liquidation rights, any distributions (including actual, constructive, or deemed distributions) that differ in timing or amount are to be given appropriate tax effect in accordance with the facts and circumstances.

Section 1.1361-1(l)(2)(iv) provides that a governing provision does not, within the meaning of § 1.1361-1(l)(2)(i), alter the rights to liquidation and distribution proceeds conferred by an S corporation's stock merely because the governing provision provides that, as a result of a change in stock ownership, distributions in a taxable year are to be made on the basis of the shareholders' varying interests in the S corporation's income in the current or immediately preceding taxable year. If distributions pursuant to the provision are not made within a reasonable time after the close of the taxable year in which the varying interests occur, the distribution may be recharacterized depending on the facts and circumstances, but will not result in a second class of stock.

Based solely on the facts submitted and the representations made, we conclude that the Agreement's provisions relating to Varying Interests Distributions, Record Date Distributions and Discretionary Payments do not cause X to have more than one class of stock for purposes of § 1361(b)(1)(D).

Except for the specific ruling above, we express or imply no opinion concerning the federal income tax consequences of the facts of this case under any other provision of the Code. Specifically, we express or imply no opinion regarding X's eligibility to be an S corporation.

This ruling is directed only to the taxpayer who requested it. Section § 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

Pursuant to the power of attorney on file with this office, a copy of this letter is being sent to X's authorized representatives.

Sincerely,

Bradford R. Poston
Senior Counsel, Branch 2
Office of the Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosures: (2)

Copy of this letter

Copy for § 6110 purposes

cc: